

D.T.E. 99-32

Petition of Fitchburg Gas and Electric Light Company for approval by the Department of Telecommunications and Energy, pursuant to 220 C.M.R. § 6.12 and the Department's Order

in D.T.E. 98-51, for an exception from the requirement to use a financing rate, through a financing vehicle or trust, in its calculations of its interest on gas inventory charges.

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FOR: FITCHBURG GAS & ELECTRIC LIGHT COMPANY

Petitioner

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Intervenor

I. INTRODUCTION

On March 15, 1999, Fitchburg Gas and Electric Light Company ("Fitchburg" or "Company") filed with the Department of Telecommunications and Energy ("Department") a petition for an exception from 220 C.M.R. § 6.06 which, among other things, requires a company to use a financing rate, through a financing vehicle or trust, in its calculations of its interest on gas inventory charges (Petition at 1).⁽¹⁾ This petition for an exception was filed pursuant to the Department's Order in Fitchburg's last gas rate case, Fitchburg Gas and Electric Light Company, D.T.E. 98-51 (1998),⁽²⁾ and 220 C.M.R. § 6.12⁽³⁾ (*id.*).

At the time of the Department's Order in D.T.E. 98-51, Fitchburg had been financing its gas inventory through cash and short term borrowings pursuant to its parent company's, Unitil Corporation ("Unitil"), Cash Pooling and Loan Agreement ("Cash Pooling Agreement")⁽⁴⁾ (Exh. FGE-1, at 5). Fitchburg then applied BankBoston's so-called "prime rate" as a proxy to calculate the interest on inventory, with all such charges recovered in its cost of gas adjustment clause ("CGAC") (*id.*). Rather than use a financing rate as established through a financing vehicle or trust, Fitchburg proposes to continue to finance its inventory costs through cash and short-term borrowings pursuant to the Cash Pooling Agreement (*id.*). However, Fitchburg proposes to calculate the proxy interest rate based on the Cash Pooling Agreement's annualized average monthly borrowing rate (including the related bank commitment fees) (*id.* at 3).⁽⁵⁾

The Company states that pursuant to the Cash Pooling Agreement, Unitil and each of its subsidiaries contribute excess funds to the cash pool with any additional funding needed to meet the requirements of its subsidiaries borrowed by Unitil through its banks (*id.*). According to the Company, any Unitil subsidiary may borrow money from the cash pool as long as the request is in line with the subsidiary's short-term borrowing limits (*id.*). Fitchburg submits that advances from the pool are made at cost with interest charges and

commitment fees based upon usage (id. at 4). Over the past year, the Company states that its average cost of borrowing from the cash pool, including related bank charges, was 6.12 percent (id.).

Pursuant to notice duly issued, the Department held a hearing on July 19, 1999. The Attorney General of the Commonwealth ("Attorney General") filed a notice of intervention as of right, pursuant to G.L. c. 12, § 11E. In support of its petition, the Company sponsored the testimony of one witness, Charles J. Kershaw, Jr., assistant treasurer of Fitchburg. The evidentiary record consists of 15 exhibits and two responses to record requests. Fitchburg and the Attorney General filed initial briefs. Fitchburg filed a reply brief.

II. POSITIONS OF THE PARTIES

A. The Attorney General

The Attorney General states that Fitchburg's proposed method of financing its gas inventory seems reasonable and agrees with the request for an exception from the Department's regulations (Attorney General Brief at 3-4). The Attorney General contends that the purpose of the Department's regulation requiring the creation of a fuel trust is to protect ratepayers from the possibility of a double collection of interest on inventory costs (id. at 3). Because there is currently no gas inventory component in rate base, the Attorney General argues that it is not necessary to establish a trust in order to protect ratepayers from double collections at this time (id.). Additionally, the Attorney General asserts that an interest rate composed of the annualized average monthly borrowing rate Fitchburg pays for borrowings from its holding company's cash pool is a reasonable proxy for financing gas inventories (id.). However, the Attorney General raises two issues concerning the implementation of Fitchburg's proposed method of financing. First, the Attorney General requests that the Department grant only conditional approval to Fitchburg's proposal to charge its customers the cash pool rate (id. at 3-4). Second, the Attorney General urges the Department to reject Fitchburg's request that Department approval of this petition be effective as of November 30, 1998 (id. at 4).

With respect to his request for conditional approval of the use of the cash pool rate, the Attorney General argues that conditional approval is necessary in order to guard against circumstances that may require the Company to return to the use of the BankBoston prime rate (id. at 3). With respect to Fitchburg's request that its proposed method of financing be made effective on November 30, 1998, the Attorney General argues that this constitutes retroactive ratemaking and is contrary to law (id. at 4). More specifically, the Attorney General asserts that Fitchburg's CGAC rates (collected from November 31, 1998 to the present), have been approved by the Department and that the Department's regulation permitting the collection of interest on gas inventory is solely prospective in nature (id.). Therefore, the Attorney General argues that making any exception from the

Department's regulations effective as of November 30, 1998, would be retroactive ratemaking that is prohibited by law absent specific statutory authorization (id.).

B. Fitchburg

Fitchburg argues that financing its fuel inventory through the Cash Pool Agreement is more cost-effective for its ratepayers than the use of a third party trust or other financing vehicle (Fitchburg Brief at 3-8). Fitchburg states that it investigated several methods for financing gas inventory, including establishing a trust to be financed either through the issuance of commercial paper or through a bank line of credit. If Fitchburg were to establish a trust, it asserts that it should be entitled to recover the monthly interest, bank fees, ongoing administrative costs, as well as the amortized amount of the initial set-up costs (Exh. FGE-1,

at 8). Fitchburg contends that recovery of these costs would considerably raise the effective interest rate charged to its ratepayers making the option of a trust much less cost-effective than the financing method the Company proposes (id. at 5, 6, 8).

Fitchburg argues that conditional approval of its proposed interest rate, as requested by the Attorney General, is neither necessary nor warranted (Fitchburg Reply Brief at 2). Fitchburg also contends that there is no record evidence to support a conditional approval (id.). In addition, the Company asserts that the Department can investigate its method of financing at any time and make changes if it finds that the approved method is no longer in the public interest (id.).

Finally, Fitchburg asserts that allowing the exception to be effective as of November 30, 1998, does not violate the stricture against retroactive ratemaking (id. at 1). Fitchburg argues that it voluntarily removed inventory interest charges from its CGAC until a financing vehicle or trust had been approved or an exception had been granted (id. at 3). Because projected inventory finance charges are a component of the CGAC, Fitchburg argues that reconciling projected charges with actual charges is not improper retroactive ratemaking (id. at 3-4). Fitchburg claims that allowing interest on gas inventory solely on a prospective basis would be contrary to the reconciling purpose of the CGAC mechanism (id. at 4). Fitchburg contends that its request to approve the proposed financing method effective as of November 30, 1998 is necessary so that the Company will know what rate to use when reconciling gas inventory costs in its next CGAC filing (id.).

III. ANALYSIS AND FINDINGS

Total inventory financing charges "shall represent an accumulation of the projected charges as calculated using the monthly average of financed inventory at the existing (or anticipated) financing rate through a trust or other financing vehicle." 220 C.M.R. § 6.06. During the investigation of Fitchburg's gas rate case, the Department found that the Company's method of financing its gas inventory did not comply with the Department's regulations contained in 220 C.M.R. § 6.06. D.T.E. 98-51, at 21. However, as noted, the Department may grant an exception from the provisions of 220 C.M.R. § 6.06 upon such terms that the exception is determined to be in the public interest. 220 C.M.R. § 6.12(1). In D.T.E. 98-51, the Department stated that, if Fitchburg petitions for such an exception, it must demonstrate that its current [proposed] financing method is more cost-effective for ratepayers than the establishment of a financing vehicle or trust. D.T.E. 98-51, at 22.

As a result of the Department's Order in D.T.E. 98-51, Fitchburg investigated the use of a trust financed through commercial paper or a bank line of credit as alternative methods for financing its gas inventory (Tr. at 8; Exh. FGE-1, at 5-6). With respect to commercial paper, that may not be an option for a company with a trust inventory as small as Fitchburg's (Tr. at 59, 62; Exh. FGE-1, at 7). Even if the Company could use commercial paper, Fitchburg has shown that the costs to establish and maintain the trust would make this method more

expensive than financing gas inventories pursuant to the Cash Pooling Agreement (Tr. at 61-62, 94; Exhs. FGE-1, at 6-8; FGE-2, Sch. B, at 1).⁽⁶⁾

Similarly, Fitchburg has shown that a third party trust funded by a line of credit is also more expensive than financing gas inventories pursuant to the Cash Pooling Agreement (Exh. FGE-1, at 7). Because Fitchburg has a relatively small trust inventory, it is likely that a bank would charge a higher rate and/or a commitment fee to administer the trust (Tr. at 75). Even if the trust could obtain a line of credit with a rate similar to the Cash Pooling Agreement, the addition of trust and legal fees would make it more expensive than Fitchburg's proposed method of financing gas inventory (Tr. at 83; Exh. FGE-2, Sch. C).

Fitchburg has demonstrated that financing its inventory through cash and short-term borrowing pursuant to the Cash Pooling Agreement is the most cost-effective option for the Company and its ratepayers.⁽⁷⁾ The Department approves the financing method proposed by Fitchburg and hereby grants the Company an exception from the provisions of 220 C.M.R. § 6.06 as in the public interest. The Department notes that we have the authority to investigate and make changes to Fitchburg's method of financing its gas inventory at any time. Therefore, it is not necessary to grant conditional approval.

Fitchburg removed inventory financing charges from its CGAC on December 15, 1998. As a result, the Company has not recovered inventory financing expenses incurred since November 30, 1998. The CGAC includes a reconciliation adjustment that allows a company to settle its projected costs to its actual costs at the time of the next peak or off-peak CGAC filing. We will permit Fitchburg to reconcile actual costs incurred at the time of the Company's next peak CGAC filing. This is consistent with the reconciliation

purpose of the CGAC and is not retroactive ratemaking. See D.T.E. 98-51, at 21 n.8. Fitchburg is, therefore, authorized to implement the proposed financing of gas costs effective as of November 30, 1998, allowing the Company to use the method of financing, and the resulting interest rate, as approved in this proceeding, in the reconciliation of gas inventory finance charges.

IV. ORDER

After due notice, hearing and consideration, it is

ORDERED: That Fitchburg Gas and Electric Light Company's petition for an exception from 220 C.M.R. § 6.06 is approved; and it is

FURTHER ORDERED: That Fitchburg Gas and Electric Light Company is authorized to implement the proposed financing of gas costs effective as of November 30, 1998.

By Order of the Department,

Janet Gail Besser, Chair

James Connelly, Commissioner

W. Robert Keating, Commissioner

Paul B. Vasington, Commissioner

Eugene J. Sullivan, Jr., Commissioner

1. This regulation requires that total inventory financing charges "shall represent an accumulation of the projected charges as calculated using the monthly average of financed inventory at the existing (or anticipated) financing rate through a trust or other financing vehicle." 220 C.M.R. § 6.06.
2. As part of that order, the Department found that Fitchburg's method of financing its gas inventory did not comply with the Department's regulations contained in 220 C.M.R. § 6.06. D.T.E. 98-51 at 21. The Department directed Fitchburg to either "petition the Department for approval of a financing vehicle or trust or to petition the Department for an exception under 220 C.M.R. § 6.12." Id. at 21-22.
3. The Department may, where appropriate, "grant an exception from the provisions of these regulations, upon such terms that it may determine to be in the public interest." 220 C.M.R. § 6.12(1).
4. The Cash Pooling Agreement was approved by the Department in Fitchburg Gas and Electric Light Company/UMC Electric Company, Inc., D.P.U. 89-66 (1992).
5. This interest rate would include the cash pool accrued interest for the month, the cash pool costs of any compensating balances, bank commitment fees and any other fees required to maintain the lines of credit (Exh. FGE-1, at 3). If Fitchburg does not borrow during any particular month, the interest rate would be calculated by adding the monthly average rate charged each cash pool participant for receiving advances from other pool participants and the pool banking costs (id.).
6. The effective annual rate for a trust financed by commercial paper (expected rate of the commercial paper, plus bank fees and amortized legal fees) was estimated to be 11.27 percent (Exh. FGE-2, Sch. B at 1).
7. Although not necessary to our finding here, Fitchburg argues that its financing proposal is likely to result in an even lower interest rate than contained in the Company's filing due to recent credit line negotiations by the Unitil on behalf of the Unitil system companies (Tr at 10-12, 31-32, 77).